



OFFICE OF THE ILLINOIS STATE TREASURER
MICHAEL W. FRERICHS

May 12, 2022

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F St. N.E.
Washington, DC 20549

Dear Secretary Countryman:

I am writing to share my views regarding the Commission's proposed rules concerning Private Fund Advisers (the "Proposed Rules"). I wanted to take this opportunity to provide comments in support of the proposals that I believe will improve transparency in the private markets and increase institutional investors' abilities as fiduciaries to meet our obligations to our beneficiaries.

As the Treasurer of the State of Illinois, I am responsible for safeguarding and prudently investing \$50 billion on behalf of taxpayers, college savers, and units of local government. I also serve as a trustee on the Illinois State Board of Investment, which manages approximately \$31 billion in assets on behalf of over 226,000 beneficiaries of a number of state retirement plans.

Private funds are significant participants in the U.S. financial system, and as a result, my office, like many other institutional investors, has been active in this space. The Illinois State Treasury makes targeted investments with venture capital, growth equity, and private venture debt funds through our \$1 billion Illinois Growth and Innovation Fund ("ILGIF"). ILGIF dollars are invested in technology-enabled businesses that are either based in Illinois or possess a significant workforce in Illinois with the goal to attract, assist, and retain these quality technology-enabled businesses in our state.

Based on my experience with private equity, I strongly support the Commission's efforts to ensure investors have access to transparent and readily comparable information about their investment opportunities, as well as improve the alignment of interest between Limited

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Partners (“LPs”) and General Partners (“GPs”). My comments, below, focus on the Proposed Rules’ provisions regarding quarterly disclosure of fees and expenses, performance disclosures, and fiduciary duty.

Fee and Expense Disclosure

Regulators have recognized the lack of transparency in this industry and have identified poor disclosures around fees and expenses.¹ For example, in June 2020, the Office of Compliance Inspections and Examinations (“OCIE”) at the Commission released a risk alert identifying numerous issues with allocation and disclosure of fees and expenses by private fund advisors that had arisen in recent compliance examinations.² OCIE noted that many of the deficiencies discussed in the risk alert may have caused investors in private funds “to pay more in fees and expenses than they should have.”³ Earlier this year, in testimony before the full Senate Banking Committee, Chair Gary Gensler stated that “[u]ltimately, every pension fund investing in these private funds would benefit if there were greater transparency and competition in this space.”⁴

Without clear and consistent disclosures, the tracking of fees and expenses charged in a private fund can be challenging for some investors. Since regular reporting on specific costs being charged to a private fund is not currently a regulatory requirement, individual investors must rely on negotiations with fund managers to secure access to this information, typically agreed through side letter agreements rather than the main governing document for a fund, known as the Limited Partnership Agreement, which outlines information granted to all investors in the fund.⁵

I am in complete agreement with Chair Gensler’s assessment that the Proposed Rules would “increase transparency and would provide comparability to fund investors.”⁶ The proposed fee and expense disclosures could “lower the cost to investors of monitoring fund fees and expenses, lower the cost to investors of monitoring any conflicting arrangements, improve the ability of investors to negotiate terms related to the governance of the fund, and improve the ability of investors to evaluate the value of services provided by the adviser and other service providers to the fund.”⁷ If the Commission moves forward with these Proposed Rules, they could improve the proposals by preserving LP-level disclosures where the adviser has agreed

¹ See, e.g., See Andrew J. Bowden, Director of OCIE, “Spreading Sunshine in Private Equity,” May 4, 2014, available at <https://www.sec.gov/news/speech/2014--spch05062014ab.html>; Marc Wyatt, Acting Director of OCIE, “Private Equity: A Look Back and a Glimpse Ahead,” May 13, 2015, available at <https://www.sec.gov/news/speech/private-equity-look-back-and-glimpse-ahead.html>.

² See U.S. Securities and Exchange Commission, Office of Compliance Inspections and Examinations, Risk Alert, June 23, 2020, available at https://www.sec.gov/files/Private%20Fund%20Risk%20Alert_0.pdf.

³ See *id.* at pg. 1.

⁴ Testimony of Gary Gensler before the United States Senate Committee on Banking, Housing, and Urban Affairs, September 14, 2021, available at <https://www.banking.senate.gov/imo/media/doc/Gensler%20Testimony%209-14-21.pdf>.

⁵ In 2020, only 8% of LPs indicated that a commitment to provide the ILPA Reporting Template was included in the LPA for all investors’ benefit; 75% indicated the commitment was typically either made through the side letter or informally and not reflected in fund documents at all. See Institutional Limited Partners Association, ILPA Industry Intelligence Private Market Fund Terms Survey (June 2020) at pg. 11.

⁶ Chair Gary Gensler, Statement on Private Fund Advisers Proposal, US Securities and Exchange Commission (February 9, 2022).

⁷ Securities and Exchange Commission, Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews, 87 Fed. Reg. 16,886 (March 24, 2022) at 16,944.

to provide them and requiring managers to provide such reporting at the request of the investor.

Performance Disclosure

I support the Proposed Rules' provisions that would require "standardized fund performance information in each quarterly statement provided to fund investors."⁸ Requiring specific transparency around performance metrics disclosed "without" the impact of any fund-level subscription facilities alongside metrics "with" the impact of subscription facilities will provide investors such as the Illinois State Treasury with a comparable and complete set of information for improved comparison.

I agree with the Commission that as a result of the proposed performance disclosures many investors:

[w]ould find it easier to obtain and use information about the performance of their private fund investments. They may, for example, find it easier to monitor the performance of their investments and compare the performance of the private funds in their portfolios to each other and to other investments. In addition, they may use the information as a basis for updating their choices between different private funds or between private fund and other investments. In doing so, they may achieve a better alignment between their investment choices and preferences.⁹

Fiduciary Duty

I am supportive of the Commission's actions to restore fiduciary duty by requiring fund advisers to be held to the same fiduciary standards as institutional investors, who themselves invest in private funds as fiduciaries on their beneficiaries' behalf. I have observed the widespread use of sole discretion language and expansive indemnification and exculpation provisions in this industry. Taken together with the growing complexity of private funds, the erosion of fiduciary duties has magnified these risks, as evidenced by the Commission's comments on persistent inadequacies in the disclosure of conflicts.¹⁰

Additionally, I encourage the SEC to clarify that any penalties or disgorgement resulting from an enforcement action that terminates in a settlement rather than a court finding will be borne by the GP and not indemnifiable.

I sincerely appreciate the time and effort that the Commission has invested in drafting these Proposed Rules. The Proposed Rules present an opportunity to enhance the ability of investors to access information critical to investment decisions while also strengthening private equity markets, which will help ensure the long-term success of the industry, establish market efficiencies, and lead to better outcomes for all stakeholders.

⁸ *Id.* at 16,900; *see id.* at 16,976.

⁹ *Id.* at 16,946-47.

¹⁰ *See, e.g.*, OCIE Risk Alert, *supra* note 2 at pg. 1-4 (observing various inadequately disclosed conflicts in examinations of registered investment advisors that manage private equity funds or hedge funds).

Thank you for your consideration.

Sincerely,

A handwritten signature in black ink that reads "Michael Frerichs". The signature is written in a cursive style with a large, stylized "M" and "F".

Michael W. Frerichs
Illinois State Treasurer